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Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	CC Docket No. 96-98
Inter-Carrier Compensation for ISP-Bound Traffic	CC Docket No. 99-68

COMMENTS OF GTE

GTE Service Corporation and its affiliated companies

Thomas R. Parker
John F. Raposa
GTE SERVICE CORPORATION
600 Hidden Ridge
HQE03J27
Irving, Texas 75038
(972) 718-6969

Gail L. Polivy
GTE SERVICE CORPORATION
1850 M Street, N.W., Suite 1200
Washington, D.C. 20036
(202) 463-5214

THEIR ATTORNEYS

April 12, 1999

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GTE Service Corporation and its below-listed affiliates[1] (collectively, "GTE") respectfully submit their Comments on the Notice of Proposed Rulemaking ("NPRM") in the above-captioned proceeding.[2] In the NPRM, the Commission seeks comment on its tentative proposal to establish a new system of inter-company compensation for circuit-switched traffic delivered to Internet Service Providers ("ISPs"). One of these proposals would delegate to states the responsibility of establishing such compensation. The alternative proposal would have the FCC establish a compensation mechanism. The Commission also invited parties to submit alternative proposals that "eliminat[e] incentives for inefficient entry and irrational pricing," enhance competition by enabling

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1 GTE Alaska, Incorporated, GTE Arkansas Incorporated, GTE California Incorporated, GTE Florida Incorporated, GTE Hawaiian Telephone Company Incorporated, The Micronesian Telecommunications Corporation, GTE Midwest Incorporated, GTE North Incorporated, GTE Northwest Incorporated, GTE South Incorporated, GTE Southwest Incorporated, Contel of Minnesota, Inc., GTE West Coast Incorporated, and Contel of the South, Inc., GTE Communications Corporation, GTE Wireless Incorporated, GTE Internetworking, and GTE Media Ventures Incorporated.

2 *Implementation of Local Competition Provisions in the Telecommunications Act of 1996 and Inter-Carrier Compensation for ISP-Bound Traffic,* CC Docket Nos. 96-98 and 99-68 (Feb. 26, 1999) ("*Ruling and NPRM*").

entry by "efficient new competitors," and benefit consumers by fostering "emerging technologies."[3]

There are compelling policy reasons why the Commission should not -- and legal reasons why the Commission may not -- simply shunt this issue to the states for resolution within the context of state arbitration proceedings. Rather, the Commission should impose an 18 month moratorium on inter-carrier compensation for ISP-bound traffic, while preserving the enhanced service providers' access charge exemption ("ESP exemption"). During that period, the Commission should develop consistent, flexible federal rules and guidelines to govern inter-company compensation for circuit-switched interstate traffic, including ISP-bound traffic. As detailed herein, these measures are needed to restore economic investment incentives and assure the continued growth of the Internet free from unwarranted regulatory intervention.

I. INTRODUCTION AND SUMMARY.

In an era when virtually any decision by the Commission is immediately questioned or challenged by one industry segment or another, there is rare and welcome unanimity in support of the agency's longstanding commitment not to regulate the Internet. This hands-off approach has been a key driver of the Internet's astounding growth and rapid assumption of a central role in global society and commerce.[4] As the Chairman recently emphasized, "[i]f you know that companies are making decisions based on marketplace incentives, rather than regulatory edicts, then you can better predict what companies will do. And more predictability and more

[3] *See Ruling and NPRM* ¶ 33.

[4] GTE, through its Internetworking affiliate, has been a major player in the development and expansion of the Internet, offering a diverse range of Internet access, backbone, web hosting, and value-added services. In addition, GTE's telephone operating companies and CLEC affiliates are leading providers of broadband access services, including a variety of xDSL offerings.

stability means: more investment, more innovation, more growth, more jobs and more opportunity."[5]

One highly successful part of the Commission's Internet-related policies has been the ESP exemption, under which information service providers can obtain interstate access without paying access charges. When first adopted in the early 1980s, this exemption was needed to avoid subjecting a nascent industry to charges well in excess of ten cents a minute on each end of a call. Over time, the exemption has enabled information service providers, and most recently ISPs, to enjoy highly efficient access to the public switched telephone network without paying the subsidies that unfortunately remain a large part of access charges paid by interexchange carriers.

GTE wishes to emphasize that it does not advocate termination of the ESP exemption at this time. GTE does, however, believe the Commission must squarely address the rampant market distortions and inequitable competitive results that have flowed from the imposition of "reciprocal" compensation obligations on ISP-bound calls that pass from ILECs (incumbent local exchange carriers) to CLECs (competitive local exchange carriers) and on to the Internet. The Commission can take immediate steps to address this matter without disturbing the ESP exemption.

The enforced payment of compensation by ILECs for ISP-bound traffic is utterly inconsistent with the Commission's fundamental desire to avoid unnecessary regulatory intrusion into the marketplace (*see* Section II herein). Forcing ILECs to pay compensation for such traffic produces an arbitrage opportunity of unprecedented magnitude in the communications industry, yielding a net outflow of hundreds of millions of dollars yearly from ILECs to CLECs, without any basis in the CLECs' costs. By cutting sweetheart deals with ISPs, CLECs create staggering traffic imbalances that not

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[5] Remarks by Chairman Kennard before Legg Mason, Washington, D.C., March 11, 1999 (as prepared for delivery).

only give them an insuperable (and unjustified) competitive advantage vis-a-vis ILECs, but have harmful spillover effects that undermine key policy goals of the Telecommunications Act of 1996 (herein "the Act" or "1996 Act).[6]

For example, CLECs have less incentive to actually provide competitive local exchange service for fear of diluting their subsidy payments from ILECs. Likewise, they are less likely to encourage high-volume customers to shift to more efficient broadband offerings such as ADSL, in order to preserve their advantageous compensation flows. For their part, ILECs are forced to write checks to CLECs using funds that could have been used to upgrade their networks and deploy new technologies.

If these revenue flows resulted from CLECs' success in the marketplace under economically rational ground rules, this matter would be of no concern to the Commission. They do not, however. Rather, they stem solely from an economically and legally indefensible arrangement unwisely thrusts the Commission into a market whose future success is imperiled by continued regulatory intervention. The situation must be corrected immediately.

The NPRM, unfortunately, does not offer a reasonable approach for doing so (*see* Section III herein). The Commission's tentative conclusion to continue allowing the states to determine whether compensation should be paid for ISP-bound traffic would simply perpetuate the plethora of harms noted above. Moreover, the Commission lacks the authority to delegate to the states its responsibility over interstate communications, including Internet access. Under Section 252 of the Act, the states are empowered to arbitrate only matters within the scope of Section 251. The Commission already has correctly determined (1) that Section 251(b)(5) requires compensation only for the transport and termination of local calls, and (2) that Internet access traffic is predominantly interstate, *i.e.*, it is not local. The states therefore have

6 Pub. L. No. 104-104, 110 Stat. 56 *codified at* 47 U.S.C. § 151 *et seq* (1996).

no authority, in the arbitration context or otherwise, to establish a compensation mechanism for Internet-bound calls.

Nor is a federal arbitration process the answer (*see* Section IV, herein). Such a process, like its state counterpart, would merely prolong and exacerbate the marketplace distortion and uncertainty created by the current regime and would be equally inconsistent with the plain language and goals of the Act. In its stead, GTE recommends a two-step solution to the reciprocal compensation problem.

First, the Commission should immediately establish an 18 month moratorium period during which no inter-carrier compensation would apply to Internet-bound calls. During this period, ILECs and CLECs alike would have to recover their own costs of delivering traffic to ISPs. The immediate cessation of compensation would put a halt to the uneconomic arbitrage and perverse investment incentives that plague the industry today and would assure ISPs and consumers alike that access charges will not be extended to the Internet.

Second, during the moratorium period, the Commission should focus on addressing long-standing issues of universal service, separations reform, and access reform, including dramatic streamlining of the Part 69 process for introducing new services. Once these items are appropriately and sufficiently dealt with, the Commission can establish a single, rational, cost-based approach to network access compensation, that applies to all interstate communications and will drive rational economical network arrangements. Specifically, under this new approach, ILECs should be permitted to make available network access arrangements to both end users (retail access arrangements) and to other carriers and ISPs (for inclusion in integrated service offerings). Such services should be made available at tariffed rates, or pursuant to negotiated agreements. The details of GTE's proposal are set forth in Section IV below.

With respect to the final issue addressed in the NPRM -- the ability of CLECs to opt into existing interconnection agreements -- GTE seeks clarification that a CLEC may not do so for a full, new contract term, but must adhere to the actual term deadlines in the original agreement (*see* Section V, herein). This outcome is compelled by the language of Section 252(i), and is necessary to avoid creating a loophole that permits CLECs to successively "renew" existing agreements into perpetuity.

II. GTE DOES NOT PROPOSE ELIMINATING THE ESP EXEMPTION AT THIS TIME, BUT RECOGNIZES THAT THE CURRENT INTER-CARRIER COMPENSATION MECHANISM FOR ISP-BOUND TRAFFIC IS CAUSING PROBLEMS WHICH SHOULD BE REMEDIED IMMEDIATELY.

GTE is not proposing that the FCC eliminate the ESP exemption at this time because that could lead to adverse consequences in the ESP market in the short term. Nonetheless, the current requirements in some states that force ILECs to make compensation payments to CLECs that handle ISP-bound traffic is leading to severe market distortions and uneconomic arrangements that must be rectified immediately.

A. Requiring Reciprocal Compensation on ISP-Bound Traffic Results In Payments That Are Not Cost-Based.

At the outset, it should be noted that costs associated with providing ISP-bound traffic, including reciprocal compensation payments, are interstate in nature, consistent with the Commission's conclusion that ISP-bound traffic is substantially interstate in nature.[7] As a result of the ESP exemption, ILECs receive no interstate revenues for delivering traffic bound for ISPs. The reciprocal compensation ILECs are required to pay CLECs for ISP-bound traffic thus represent costs associated with the provision of an interstate service for which ILECs receive no interstate revenues -- essentially, ILECs are expected to make these payments out of funds that does not exist, either at the interstate or the state level.

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[7] *See Ruling and NPRM* ¶¶ 18, 20.

On average, an ILEC charges a flat rate of approximately $20 for local service each month. Under a reciprocal compensation scheme, whenever an ILEC end user is connected to an ISP through a CLEC, the CLEC is entitled to payments for every minute the connection is maintained. Calls to an ISP typically make use of local switching facilities for significantly longer periods than the average holding time for local telephone calls. Since reciprocal compensation charges are usage-based, it does not take much usage for the reciprocal compensation payments to dwarf the flat fee the originating customer pays the ILEC.[8] In GTE's territories, this scenario has resulted in claims for millions of dollars of compensation.

Worse yet, the size of these payments is wholly unrelated to the functions performed by the CLEC. Recent technological developments have made it possible for some CLECs to avoid circuit-switching on ISP-bound traffic. New SS7 bypass devices, for example, permit calls to selected telephone numbers (*e.g.*, ISPs) to be directly transported to their destination, thereby avoiding circuit-switching altogether.[9] According to media descriptions, this can reduce a carrier's costs by a factor of ten.[10] Furthermore, new technologies will make it easier for ISPs to terminate calls without having to use traditional switching.

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8 An ISP's heaviest users can generate reciprocal compensation payments that far exceeds the flat rate paid to the ILECs. Such users may average five hours of on-line time each day. At the typical reciprocal compensation level of half a cent ($0.005) per minute, these heavy users would generate as much as *$45.00 per month* in reciprocal compensation claims, compared to the typical $20.00 per month flat rate for residential service.

9 *See ISPs Strongarm GTE; UUNet, Others Demand SS7 Bypass Savings*, ISP Business News, November 9, 1998, at 1 (describing SS7 bypass equipment manufactured by Ascend Communications) ("*ISPs Strongarm GTE*"); *see also* Competitive Carrier Strategies II Workshop, Ascend (visited Apr. 6, 1999) <http://www.ascend.com/3536.html> (offering seminars suggesting "Solutions for turning recent regulations [including the FCC reciprocal compensation decision] into profit opportunities.").

10 *See ISPs Strongarm GTE* at 1.

Allowing CLECs to recover reciprocal compensation for delivery of ISP-bound calls in such a manner grossly overcompensates them and constitutes a massive cash windfall.[11] This disparity is exacerbated by the fact that CLEC networks (even without SS7 bypass) are far less complex and utilize fewer switches than ILECs' networks. While standard voice calls handled by ILECs often pass through multiple switches before final delivery, traffic handled by CLECs in the manner described above may involve no circuit-switching at all. Thus, compensating CLECs based on an ILEC's costs aggravate the subsidy these carriers already enjoy in delivering traffic to ISPs.

B. The Perverse, Uneconomic Incentives of the Current System Harm Competition and Consumers.

1. CLECs Have Achieved an Unwarranted Competitive Advantage.

Evidence from the marketplace proves that shoe-horning ISP-bound traffic into the local reciprocal compensation framework has produced uneconomic results. Most notably, many CLECs are willing to offer deeply discounted access, or free access, to entice ISPs to locate behind them in order to "generate" reciprocal compensation payments from LECs.

In a recent submission to the New York Public Service, Bell Atlantic offered a host of examples of such artificially sweetened deals offered by CLECs in New York

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[11] A recent case before the Texas State Public Utilities Commission involved a similar traffic arrangement. That case involved a Texas company, CT Cube, that delivered end user traffic to an ISP. It routed traffic using DS-1s directly to its ISP router without going through its switch. The Texas PUC held that CT Cube was not entitled to reciprocal compensation because it did not provide any switching function -- and could just as easily hook directly to the local ILEC's switch. Thus, the Texas PUC denied CT Cube reciprocal compensation on grounds that to do otherwise "is to invite . . . providers to engage in uneconomic investment for the purposes of receiving [reciprocal compensation]." Public Utility Commission of Texas Arbitrator's Decision, Petition for Arbitration Pursuant to FTA § 252(b) to Establish an Interconnection Agreement with GTE Southwest Incorporated, PUC Docket No. 20028 at 13 (Feb. 22, 1999).

State.[12] Indeed, analysts have reported that "the vast majority of CLEC reciprocal compensation claims – possibly as high as 80-90% of the claims—are for the termination of traffic related to dial-up [I]nternet access and not for voice services."[13] According to this report, if the growth of reciprocal compensation remains unchecked, the total of ILECs obligations "will grow to $2.1 billion by 2000."[14] In the words of one industry analyst, reciprocal compensation for Internet traffic is "arguably the single greatest arbitrage opportunity and hence market distortion in the telecom sector today," because "companies reap as much as 4,000 percent arbitrage for minimal, value-added service."[15] One CLEC, US LEC, estimated that reciprocal compensation accounted for two-thirds of its total corporate revenues in 1998.[16] Electric Lightwave, Inc. also reported that reciprocal compensation accounted for approximately 20% of its 1998 revenues.[17]

The subsidization represented by reciprocal compensation for ISP-bound traffic thus confers on CLECs an unwarranted competitive advantage. If inter-carrier compensation were designed merely to cover the costs of carrying traffic, there logically

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12 *See In the Matter of ACC National Telecom Corp. Blocking Obligations for Chatline Services*, New York State Public Service Commission, Case No. 98-C-1273, Bell Atlantic - New York's Comments at 7-9 (filed March 15, 1999). For example, Bell Atlantic referenced several reports that CLECs are offering to share reciprocal compensation revenues with ISPs (*i.e.*, offering *cash back*), and a quote from a Buffalo-area ISP executive boasting that "[e]very single ISP . . . in Buffalo is in on this deal." *Id.* at 7-9.

13 "Telecom Services—Local: The Mysterious World of ISP-Related Reciprocal Compensation," In-depth Report, Merrill Lynch & Co., Global Securities Research & Economics Group, at 14 (October 27, 1998) ("*Merrill Lynch Report*").

14 *Id.* at 11.

15 Scott C. Cleland, The Precursor Group/Legg Mason Research Technology Team, *Reciprocal Comp for Internet Traffic -- Gravy Train Running Out of Track* (June 24, 1998).

16 *See* US LEC Corp. SEC 10-K filing for March 31, 1999, *available at* <http://www.sec.gov/Archives/edgar/data/1054290/0000950168-00-001009/txt>.

17 *See* Electric Lightwave, Inc. SEC 10-K filing for March 5, 1999, *available at* <http://www.sec.gov/Archives/edgar/data/1044827/0001044827-99-000003.txt>.

would be no inherent, systemic reason for ISPs to choose one class of carrier over another -- rather, decisions would be made on competitive criteria. In the words of one CLEC, the reciprocal compensation mechanism merely represents a "niche opportunity related to the asymmetrical traffic patterns under Federally mandated Interconnection architecture."[18] CLECs are in a position to exploit the advantage conferred by the uneven compensation scheme because they have the freedom to offer a full range of special deals to ISPs, unlike ILECs, which are subject to heavier regulation and are not free to offer similar deals. The Commission should not tolerate or perpetuate such economic distortion.

2. The Current Compensation Scheme Undermines Key Goals of the 1996 Act.

These distortions in the Internet access market have spillover effects that directly undermine fundamental policy goals of the 1996 Act. Specifically, because LECs with customers who use the Internet incur significant liabilities as a result of the reciprocal compensation mechanism, CLECs face a sizable disincentive to actually provide basic local service to end users. This undermines Congress' intent to promote consumer choice and competition in local telephone markets.

The current regulatory approach also does not provide proper incentives for carriers to deploy and use broadband technology, because it favors dial-up access over other forms of access. Based on the revenue flows that exist under a reciprocal compensation arrangement for circuit-switched ISP-bound traffic, CLECs and ISPs have little incentive to migrate heavy users off of the dial-up, circuit-switched network onto new services such as xDSL. To the contrary, CLECs actually have incentives to

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[18] *Matter of Petition of XCOM Telephony, Inc. for a Certificate of Public Convenience and Necessity to Provide Switched and Dedicated, Resale and Facilities-Based, Interexchange and Local Exchange Telecommunications Services Throughout the State of New York*, New York State Public Service Commission, Case No. 97-C-1531, Petition (filed September 5, 1997).

attract heavy users to this medium, as they receive reciprocal compensation in excess of their actual expenses for each minute a customer remains logged onto the Internet.

This arbitrage arrangement harms customers of ILECs by uneconomically diverting funds that could be used to upgrade networks and implement new technologies. Incumbents typically receive from their basic service subscribers only a discrete, flat monthly payment, but are obliged to pay usage-sensitive reciprocal compensation charges for that subscriber's Internet calls. These usage-sensitive charges will often substantially exceed the subscriber's flat monthly payment for local service,[19] draining away revenues from services that often are already priced below cost.

III. THE COMMISSION MAY NOT DEFER THIS INTERSTATE MATTER TO THE STATES.

In the NPRM, the Commission tentatively concludes that states should continue to handle the issue of reciprocal compensation for ISP-bound traffic, even though this traffic is jurisdictionally interstate.[20] As discussed herein, this proposal is fundamentally at odds with the Communications Act.[21]

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19 *See, supra* at note 7. Moreover, CLECs will have every incentive to encourage Internet users to maintain even longer Internet connections, since they will continue to collect reciprocal compensation in excess of their actual expenses for each minute a customer remains logged onto the Internet.

20 *See Ruling and NPRM* ¶ 30.

21 GTE elsewhere has recommended that the states be given plenary ratemaking authority over services provided over local access facilities. *See Jurisdictional Separations Reform and Referral to the Federal-State Joint Board*, CC Docket No. 80-286, Comments of GTE (filed March 30, 1999). Until the Commission adopts GTE's proposal in the separations docket, the dual jurisdictional framework continues to apply, however, and interstate service remains a matter squarely under the Commission's jurisdiction. GTE is arguing here that the Commission may not simply single out *one* type of interstate service and transfer regulatory authority over that interstate service to the states until more fundamental separations reform is implemented.

A. The Commission's Conclusion that States May Extend Reciprocal Compensation Obligations to Cover ISP-Bound Traffic Is Inconsistent with the Communications Act.

1. Sections 251 and 252 Do Not Confer Authority On The States To Arbitrate Reciprocal Compensation Issues Relating To Interstate Traffic.

Sections 251 and 252 of the 1996 Act impose a finite set of interconnection obligations on ILECs. Among these obligations is the "duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications."[22] The Commission has made it clear that an ILEC's duty to provide reciprocal compensation applies only to "interconnected local traffic,"[23] and not to interstate traffic.[24] According to the Commission's own words, "ISP-bound traffic is non-local interstate traffic" and, therefore, "the reciprocal compensation requirements of section 251(b)(5) of the Act . . . do not govern inter-carrier compensation for this traffic."[25]

Nonetheless, the Commission suggests that "the mere fact that ISP-bound traffic is largely interstate does not necessarily remove it from the section 251/252 negotiation and arbitration process."[26] This is patently wrong. A plain reading of these sections indicates that state commissions may only arbitrate issues relating to an ILEC's interconnection obligations, and nothing more. Specifically, Congress authorized arbitration only on the "issues set forth in [a party's] petition and in the response."[27] These petitions, in turn, may address only the "unresolved issues" or "open issues" left

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22 47 U.S.C. § 251(b)(5).

23 *Ruling and NPRM* ¶ 26 n.87.

24 Indeed, the entirely separate inter-carrier compensation system of access charges applies to non-local, interstate traffic. *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, 11 FCC Rcd 15499, 16012-13 (1996).

25 *Ruling and NPRM* ¶ 26 n.87.

26 *Id.* ¶ 25.

27 47 U.S.C. § 252(b)(4)(A).

over from the negotiation process.[28] ILECs are only obliged to negotiate "the particular terms and conditions of agreements to fulfill the duties described in [Sections 251 (b) and (c)]."[29] Because Section 251(b)(5) does not require ILECs to provide reciprocal compensation for ISP-bound traffic, this matter is beyond the scope of the negotiation process and, therefore, is not within the scope of a state commission's authority.

Other provisions within Section 252 confirm that state commissions may not arbitrate interstate matters that are not explicitly covered by Sections 251. In this regard, Section 252(c) provides that a state commission is required to ensure that any resolution of "open" or "unresolved" issues meet the requirements of Section 251 -- which means that reciprocal compensation arrangements derived from Section 251(b)(5) must exclude ISP-bound traffic. Section 252(d)(2) provides specific standards for state commissions in determining if the terms and conditions for reciprocal compensation *pursuant to Section 251(b)(5)* are just and reasonable. Finally, Section 252(e)(2) provides specific grounds upon which a state commission may reject an interconnection agreement adopted by arbitration. Unlike voluntarily negotiated interconnection agreements, which may include issues not explicitly identified in Section 251(b), interconnection agreements adopted by arbitration can only be rejected on grounds that the agreement does not meet the requirements of Sections 251 and 252 or the related regulations.

To be sure, interconnecting carriers are entitled to seek interconnection "without regard to the standards set forth in subsections (b) and (c) of section 251," and request that LECs take steps that go beyond the duties enumerated in these sections.[30] To suggest that parties may petition states to arbitrate issues beyond the scope of an

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28 *See id.* §§ 252(b)(1) and (b)(2)(A).

29 *Id.* § 251(c)(1).

30 *Id.* § 252(a)(1).

ILEC's duties under the Act would effectively read the limits placed on an ILEC's interconnection obligations right out of the Act. Indeed, under this interpretation, nothing would stop a party from requesting arbitration concerning reciprocal compensation of *other* interstate services -- or any other interstate issues, such as access charges -- and nothing would stop states from forcing LECs to accept an agreement including such terms. Quite simply, the Act does not authorize state commissions to use the arbitration process to expand an ILEC's statutory interconnection obligations.

2. The Commission's Regulatory Authority Over Interstate Traffic Cannot Be Delegated to The States.

In the *Ruling and NPRM*, the Commission properly concluded that ISP-bound traffic is substantially interstate in nature.[31] Section 201(a) grants exclusive jurisdiction over interstate communications -- including the terms of inter-carrier compensation for ISP-bound traffic to the Commission.[32] Moreover, the courts have long recognized the

[31] The Commission explained that, for jurisdictional purposes, it assesses ISP-bound traffic on an end-to-end basis, rather than parsing such traffic into a local "access" segment and a separate interstate "information" or "Internet" segment. *Ruling and NPRM* ¶ 13. In an analogous setting, and applying the same "end-to-end" jurisdictional analysis of ISP-bound traffic, the Commission has concluded that several ILECs' ADSL service which allows end-users to connect to ISPs via a dedicated line (rather than via a traditional dial-up connection) is jurisdictionally interstate in nature and is properly tariffed at the federal level. *See GTE Tel. Operating Cos, GTE Transmittal No. 1148,* CC Docket No. 98-79, FCC 98-292, Memorandum Opinion and Order (Oct. 30, 1998) ("*GTE ADSL Order*"), *petitions for reconsideration denied, GTE Tel. Operating Cos, GTE Transmittal No. 1148,* CC Docket No. 98-79, FCC 99-41, Memorandum Opinion and Order (Feb. 26, 1999) ("*GTE ADSL Reconsideration Order*"); *see also Bell Atlantic Telephone Cos.* CC Docket No. 98-168; *BellSouth Telecommunications, Inc.*, CC Docket No. 98-161; *GTE System Telephone Cos.*, CC Docket No. 98-167; and *Pacific Bell Telephone Co.*, CC Docket No. 98-103, FCC 98-317, Memorandum Opinion and Order (Nov. 30. 1998). Specifically, the Commission stated that "the communications at issue here do not terminate at the ISP's local server . . . but continue to the ultimate destination or destinations, specifically at a Internet website that is often located in another state." *Ruling and NPRM* ¶ 12.

[32] Specifically, this section authorizes the Commission to require common carriers to "establish physical connections" and "through routes" and to fix the access "charges applicable thereto and the divisions of such charges." 47 U.S.C. § 201(a). Also, in Section 201(a), Congress grants the Commission jurisdiction over "all interstate and
(Continued...)

essential jurisdictional divide between state regulation of intrastate communications and federal regulation of interstate matters and have cautioned that states may not regulate interstate communications.[33]

The Commission cannot simply disclaim its interstate responsibilities, or delegate them to the states. The Commission has a statutory obligation to regulate "interstate and foreign commerce in communication[s]."[34] Sections 151 and 201 "fence off" the states' authority to regulate interstate matters. The Commission cannot circumvent this statutory boundary by delegating or disclaiming its interstate regulatory obligations to the states.

B. The Commission's Decision To Exempt ISPs From Payment Of Access Charges Does Not Mean That States May Require Reciprocal Compensation For ISP-Bound Traffic.

In the NPRM, the Commission suggested that, absent a rule directly addressing the specific issue of inter-carrier compensation for ISP-bound traffic, its "policy of treating ISP-bound traffic as local for purposes of interstate access charges would, if applied in the separate context of reciprocal compensation, suggest that such compensation is due for that traffic."[35] Requiring reciprocal compensation for ISP-

(...Continued)
foreign communication by wire." 47 U.S.C. § 152(a).

33 *See, e.g., Ivy Broadcasting Co. v. AT&T*, 391 F.2d 486, 491 (2nd Cir. 1968) ("questions concerning the duties, charges and liabilities of telegraph or telephone companies with respect to interstate communications service are to be governed solely by federal law and . . . the states are precluded from acting in this area"). In reaching its conclusion, the Second Circuit recognized that Congress had enacted a broad scheme for the regulation of interstate service, and had intended to "occupy the field" to the exclusion of the states. *Id. See also AT&T Corp. et al. v. Iowa Utilities Board*, __ U.S. __, 119 S.Ct. at 732-733 (1999) (confirming that the Commission's general authority under Section 201(b) to carry out the provisions of the Communications Act includes jurisdiction over "interstate and foreign communications").

34 47 U.S.C. § 151; *see also* 47 U.S.C. § 201(a) (conferring authority on the Commission to regulate "common carrier[s] engaged in interstate or foreign communication by wire or radio").

35 *Ruling and NPRM* ¶ 25.

bound traffic is not, however, a logical extension of the ESP exemption. Quite the opposite, the Commission's decisions creating and renewing this exemption of necessity indicate that ESP traffic is jurisdictionally interstate.[36]

The Commission's decision to exempt the ESPs from access charges did not hinge on a determination that ISP-bound traffic is local. In fact, the Commission held that "ISPs should not be required to pay interstate access charges" *notwithstanding* the fact that they "may use incumbent LEC facilities to originate and terminate interstate calls." No exemption would have been necessary had the Commission determined that such traffic is local, because there is no question that access charges do not apply to local calls.[37]

C. The Commission Should Not Divide ISP-Bound Traffic Into "Interstate" and "Intrastate" Elements.

The NPRM properly does not suggest that states have jurisdiction over ISP-bound traffic based on a division of such traffic into a local "access" segment and an interstate "Internet" segment. Nor can arguments to this effect be credited. Such a two-call approach would constitute a stark reversal, as the FCC has consistently held that ISP-bound traffic will be analyzed on an end-to-end basis. Abandoning the end-to-end approach at this time would call into question the validity of the Commission's

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36 The Commission *is* correct, however, that "[its] determination that at least a substantial portion of dial-up ISP traffic is interstate does not . . . alter the current ESP exemption." *Ruling and NPRM* ¶ 20.

37 Moreover, before making the exemption "permanent" in 1997, the Commission repeatedly suggested that it was going to lift the exemption and apply access charges to ISP-bound traffic. This it could not do if ISP-bound traffic were actually intrastate. *See e.g., Amendments of Part 69 of the Commission's Rules Relating to Enhanced Service Providers,* 64 RR 2d 1294 (April 27, 1988) and *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing Usage of Public Switched Network by Information Service and Internet Access Providers,* 11 FCC Rcd 21354 (Dec. 24, 1996).

longstanding precedent, upheld by a consistent line of appellate court rulings.[38] These holdings were sound and should not be disturbed.[39]

The only possible theoretical basis for splitting jurisdiction over ISP traffic would be based on an assessment of Internet traffic itself -- allowing states to regulate the compensation mechanisms for Internet traffic that stays exclusively intrastate (on an end-to-end basis), and recognizing federal jurisdiction over all other Interstate traffic. Such an approach, however, would be technically infeasible and ill-advised.[40]

Due to the nature of the Internet protocol and the way users utilize the Internet, Internet traffic cannot be reasonably separated into jurisdictional categories. Indeed, the Commission's Office of Plans and Policy has acknowledged that Internet traffic "has no built-in jurisdictional divisions."[41] This is due, in large part, to the fact that an individual Internet session usually does not have a single destination:

> [B]ecause the Internet is a dynamically routed, packet-switched network, only the origination point of an Internet

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[38] *See GTE ADSL Order* ¶ 17; *Petition for Emergency Relief and Declaratory Ruling Filed by the BellSouth Corp.*, 7 FCC Rcd 1619, 1621 (1992) (quoting *New York Tel. Co. v.* FCC, 631 F.2d 1059, 1066 (2d. Cir. 1980); *Puerto Rico Tel. Co. v. FCC*, 553 F.2d 694, 699 (1st Cir. 1977); *MCI Communications Corp. v. AT&T*, 369 F. Supp. 1004, 1028-1029 (E.D. Pa. 1974), *vacated on other grounds*, 496 F.2d 214 (3d Cir. 1974).

[39] Treating the "dial-up" segment as "local" is not only legally and logically irreconcilable, but also does violence to the principle of technological neutrality. ADSL access and dial-up access are functionally equivalent -- both allow end users access to the Internet. It makes no sense to establish a federal scheme governing apportionment of costs between interconnecting carriers for one of these access services, and a separate state scheme for the other.

[40] The Commission did state that "ADSL services may be appropriately tariffed as intrastate services" where customers' Internet use is 10% or less interstate. *See GTE ADSL Reconsideration Order* ¶ 4. GTE does not suggest that states lack regulatory authority over Internet traffic that is demonstrated to be purely intrastate in nature. Indeed, in the ADSL Tariff proceeding, GTE readily offered to seek state tariffing for customers that will not use the Internet for interstate purposes. However, as explained below, GTE submits that it would be difficult or impossible to separate Internet traffic into different compensation schemes overseen by different jurisdictions on a session-by-session, or a website-by-website basis.

[41] Kevin Werbach, *Digital Tornado: The Internet and Telecommunications Policy*, OPP Working Paper No. 29, at 45 (Mar. 1997) ("*Digital Tornado*").

> connection can be identified with clarity. Users generally do not open Internet connections to "call" a discrete recipient, but access various Internet sites during the course of a single connection.[42]

Thus, a single Internet session may be intrastate, interstate, *and* international. Indeed, not only can an Internet session involve multiple sequential sites, the sites may also be accessed simultaneously.

Even if the Commission were determined to sort out the jurisdictional nature of each Internet communication, the traffic carried over an Internet access arrangement cannot be jurisdictionally identified as a technical matter:[43]

> Internet routers have also not been designed to record sufficient data about packets to support jurisdictional segregation of traffic.[44]

Absent the ability to segregate this Internet traffic,[45] there is no basis for a broad finding that ISP-bound traffic is anything but interstate in nature.

IV. THE COMMISSION SHOULD ESTABLISH A SINGLE, RATIONAL COST-BASED APPROACH TO NETWORK ACCESS COMPENSATION THAT APPLIES TO ALL INTERSTATE COMMUNICATIONS.

Plainly, there is no legal or policy basis for perpetuating the current system under which ILECs compensate CLECs for forwarding calls to ISPs. Merely replacing the

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42 *Id.*

43 In some ways, this situation is similar to the "leaky PBX" phenomenon, whereby interstate traffic from the local PBX cannot be specifically identified but is nonetheless subject to access charges because of the technical inability to segregate these calls. *MTS and WATS Market Structure*, Memorandum Opinion and Order, 97 FCC 2d 682, 868-70 (1983). The Commission has termed this decision a "pragmatic accommodation to measurement difficulties." *Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture*, 4 FCC Rcd 3983, 3989 (1989).

44 *Digital Tornado* at 45.

45 Obviously, where such traffic is severable, allocations between the state and federal jurisdictions may be performed. *See, e.g., Determination of Interstate and Intrastate Usage of Feature Group A and Feature Group B Access Service*, 4 FCC Rcd (Continued...)

current system, where this obligation is unlawfully imposed through the state arbitration process, with a federal arbitration process is not the answer. Marketplace distortions and unwarranted subsidies would persist, and the compensation system arbitrarily would continue to depend on whether a call is directed to an IXC or an ISP.[46]

GTE sets forth below its recommended solution, which contains an interim and a longer-term component. In the interim, as explained in subsection A, the Commission should impose an 18 month moratorium on inter-carrier compensation for ISP-bound traffic. Following the moratorium period, the Commission should establish a cost-based compensation system as described in subsection B.

A. The Commission Should Impose An 18 Month Moratorium On Inter-Carrier Compensation For ISP-Bound Traffic.

To stem the harms cited above and prevent future distortions, the Commission should immediately impose an 18 month moratorium on inter-carrier compensation for ISP-bound traffic. Until the end of this period, there would be no compensation for ISP-bound traffic paid by ILECs to CLECs, or by CLECs to ILECs. Notably, this moratorium will not prevent CLECs from being compensated; they are free to charge ISPs for the traffic they deliver under their current agreements. Furthermore, CLECs will be free to enter into new, prospective agreements with ISPs that provide appropriate compensation for costs associated with delivery of traffic.

The Commission's tentative decision to shunt this problem off to the states for resolution through the Section 252 arbitration process is not an effective response and

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8448 (1989).

[46] Such disparate treatment is becoming increasingly untenable as the traditional features distinguishing IXCs and ISPs, and the services these carriers provide, continue to blur.

is far inferior to a moratorium.[47] Simply delegating this issue to the various state commissions would allow the conditions discussed above to worsen and would further entrench the inefficient behavior and network configurations that already plague the industry.

The 18 month moratorium period proposed by GTE will allow ISPs the time to begin to make decisions regarding their networks that are based on efficiency, customer demand and market conditions, rather than on artificially-sweetened deals from CLECs. ISPs also will be motivated to create new end user Internet access offerings that incent the heaviest end users to migrate away from circuit switching to ADSL or cable modem service.[48] Indeed, some ISPs have already begun to design their end user offerings to cater to the usage amounts of their customers.[49]

B. The Proposed Moratorium Affords the Commission Time to Implement Much-Needed and Long-Overdue Regulatory Reforms.

During the moratorium period, the Commission should focus on addressing long-standing issues of universal service and access reform -- including dramatic streamlining of the Part 69 process of introducing new services. Once these items are appropriately and sufficiently dealt with, the Commission can establish a single, rational

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47 Moreover, this approach requires parties to negotiate and/or arbitrate inter-carrier *payments* -- but does not address where these funds will come from. The issue of inter-LEC compensation cannot be addressed in isolation from the rest of the pricing framework. Indeed, even if LECs are permitted to negotiate, how can they determine how they will compensate each other if they don't know how much, or whether, they will be able to recover from other entities? At present, if LECs are required to pay reciprocal compensation for this interstate traffic, they have no corresponding interstate revenues, whether from end users or from ISPs.

48 During this period, ISPs should be allowed maximum flexibility to develop new products and access arrangements. Without open access to cable modem networks, only a small subset of ISPs will be able to truly respond to customers' needs.

49 For example, MindSpring offers end users three different flat pricing plans based on usage: (1) 5 hours a month, plus a per-hour charge for usage exceeding 5 hours; (2) 20 hours a month, plus a per-hour charge for usage exceeding 20 hours; and (3) unlimited usage per month for a higher flat price. *See* MindSpring website, (visited

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approach to all forms of interstate network access that ILECs provide – to ISPs as well as to IXCs. The Commission has opened a number of dockets to address these issues in serial fashion. What is needed now is action by the Commission in the upcoming months on all of the network access issues in an integrated fashion so that the question of inter-LEC compensation can then be addressed.

GTE does not propose simply eliminating the ESP exemption and imposing current access charges on ISPs. Today's access charges are burdened with implicit universal service subsidies, and the current access charge rules are too rigid to permit ILECs to offer services that meet the needs of ISPs in an efficient way.

Instead, GTE recommends that the Commission develop a network access regime that would 1) allow all LECs to be compensated for their costs of delivering traffic; 2) treat similar uses of the ILECs' networks in a consistent way, promoting efficient competition in markets for local, long distance, and information services; and 3) provide consumers with the broadest possible choice of service options.

1. The Commission Must Adopt a More Rational Network Access Framework Before the Issue of Inter-LEC Compensation Can Be Addressed.

The question of how ILECs and CLECs should compensate one another should be dealt with *after* the more fundamental issues of network access have been addressed. In this proceeding, the Commission seeks comment on rules for inter-LEC compensation, but defers the issue of how ISPs or end users will pay for the network access they use. Until the question of how end users and service providers will compensate LECs has been settled, it is not possible to determine what payment, if any, should be made between LECs involved in such transactions. Attempting to resolve inter-LEC compensation first is to put the cart before the horse.

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Apr. 8, 1999) <http://register.mindspring.com/cgi-bin/wsisa/dll/signup/signup1.w>.

Ultimately, the revenue that covers the costs of all telecommunications and information services comes from end users. As the Notice recognizes (*Ruling and NPRM* ¶ 89), when an end user purchases a service provided by more than one carrier or service provider, there are several possible frameworks through which the end user may compensate the different parties. These different approaches coexist in the marketplace today, and they fall very broadly into two categories:

- The "service provider pays" model. Under this approach, an end user purchases an integrated service package from a service provider. This service "packager" buys at wholesale any telecommunications services necessary to put together the retail package. The end user pays the packager for the service, and the packager then pays, or shares revenue with, the underlying telecommunications providers. Most interstate long distance service works this way: an IXC purchases access from LECs at both ends of a call, and bills its end user for the integrated service.

- The "customer pays" model. Rather than purchase an integrated service package, the end user may pay the LEC that provides its connection to the network to reach another customer or service provider. If the LEC that receives revenue from the end user passes the traffic to a second LEC, it then shares that revenue with the other LEC. This is the typical approach used for local traffic.[50]

Clearly, the appropriate pattern of any inter-LEC compensation depends upon how the end user chooses to purchase service, and how the end user and/or the service provider compensate the LECs. If the end user pays for the service, then revenue flows through the LEC that serves the end user to any interconnecting carriers; if the service provider pays for the service, then revenue flows through the LEC that connects with the service provider back to any interconnecting carriers.

The problem with the Commission's current policies is that they are not consistent with either model. ILECs do not charge end users to reach ISPs, nor do they charge ISPs to reach end users. In effect, the Commission has chosen the "nobody pays" model. This state of affairs cannot be maintained in a competitive market, since,

50 The "end user pays" model also applies when an end user purchases special access to reach an IXC.

as the Notice recognizes, LECs do incur costs to switch and transport traffic bound for ISPs. Since there is no interstate revenue associated with the interstate service of transmitting ISP-bound traffic, there is no revenue to be shared between ILECs and CLECs. The Commission must act to correct this unsustainable approach.

2. The Integrated Framework For Network Access Arrangements Should Provide New Service Options for Customers.

In order to promote the development of an efficient, integrated system of interstate network access arrangements, the Commission must adopt a revised set of rules that avoid the rigid prescription of the Commission's current access charge rules. These rules should provide a framework within which ILECs may develop and offer network access options to their customers – IXCs, ISPs, and end users. The new framework should have the following features:

- The new rates for network access must not be burdened by the implicit subsidies that are generated by today's access rates. The Commission should take prompt action to replace these implicit support flows with explicit universal service funding. This will allow the rates for network access to fall to more economically efficient levels.
- ILECs should be able to offer a variety of service and pricing options to their network access customers. For example, customers should be allowed to choose circuit-switched offerings, existing special access arrangements, or newer dedicated services, such as ADSL. Customers also should be able to take service under different pricing packages, such as volume discounts or flat-rated options. To allow such options to be offered, the Commission must dramatically streamline its rules for reviewing new access services. The current system has delayed the introduction of new services by months, and sometimes years.[51]
- Different arrangements may be designed to meet the needs of ISPs and/or IXCs, who may pay different rates for different arrangements. In no event, however, should the price depend on the purchaser's regulatory classification.
- In general, these options should be wholesale offerings and would follow the "service provider pays" model, because both IXCs and ISPs will wish to

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[51] For example, GTE filed a petition for waiver to implement Zone Plus in November, 1995. The Commission has yet to issue a decision on this petition.

package complete retail services for their customers. However, the rules should also allow ILECs to develop retail offerings of their own, for their end-user customers who may wish to purchase access directly from their local carrier. Compensation for such end user offerings would follow the "end user pays" model. The Commission's current access rules should be relaxed to allow such retail interstate access services.

- ILECs should be permitted to offer these service arrangements pursuant to tariff or negotiated agreements. While the Notice correctly concludes that "a negotiation process, driven by market forces, is more likely to lead to efficient outcomes than are rates set by regulation,"[52] the Commission's current access rules do not allow ILECs to negotiate agreements with IXCs for access.

These principles will increase the availability of different service options for customers and permit the market to act in more competitive ways.

V. THE COMMISSION SHOULD CLARIFY ITS "MOST FAVORED NATION" REQUIREMENT.

Section 252(i) requires ILECs to make available to requesting telecommunications carriers any individual interconnection, service, or network element arrangement contained in any state-approved interconnection agreement arbitrated under Section 252, on the same rates, terms, and conditions as those provided in the agreement. *See* 47 U.S.C. § 252(i); 47 C.F.R. § 51.809. In paragraph 35 of the NPRM, the Commission noted that a state commission recently has allowed a party, pursuant to Section 252(i) to opt into an existing agreement for a full, new contract term, rather than adhere to the actual term deadlines in the original agreement. The Commission acknowledged the possibility that this interpretation of Section 252(i) could "rais[e] the possibility that the incumbent LEC might be subject to the obligations set forth in that agreement for an indeterminate length of time, without any opportunity for renegotiation, as successive CLECs opt into the agreement." GTE shares the Commission's concern, and urges the Commission to clarify that such an interpretation

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52 *Ruling and NPRM* ¶ 29.

is in error, and that parties opting into agreements under this section are bound by the original terms of the agreement.

A plain reading of Section 252(i) does not support the state arbitrator's interpretation expressed above. Section 252(i) mandates only that the *same* terms and conditions as are contained in approved agreements be made available. A request for a different expiration or termination date, however, changes the entire nature of the arrangement and in fact it constitutes *different* terms and conditions than in the approved arrangement -- and, thus, is not covered under Section 252(i). Indeed, offering service under carefully negotiated terms, prices and conditions from 1997 until 2000 is very different from offering the same provisions for an additional year, or two, or twenty. For example, a LEC that knows that it intends to implement a major system change in 2000 would certainly negotiate different provisions knowing that the change would take effect during the contract, or after it expires.

Failure to limit Section 252(i) in this manner would effectively enable one carrier after the other to create a "daisy chain" of successive adoptions, renewing and extending the contract term into perpetuity. As the Commission has already noted, such daisy chain adoptions might cause ILECs to "be subject to the obligations set forth in the [original] agreement for an indeterminate length of time, without any opportunity for renegotiation, as successive CLECs opt into the agreement."[53] Such daisy chains would seriously inhibit, and in fact would discourage, development of new technologies and economically efficient business practices. Negotiation of interconnection agreements would come to a halt as ILECs would be unable to agree to any provision out of a very legitimate fear that any agreement would create an obligation that exists in perpetuity.

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[53] *Ruling and NPRM* ¶ 35.

The Commission should further clarify that an ILEC is not required to make available individual arrangements contained in agreements that are so close to expiring that they have entered the designated renegotiation period.[54] Unless carriers are permitted to opt into agreements under "refreshed" contract terms (which they should not be allowed to do) it would make little sense to allow a carrier to opt into an almost-expired contract, only for its final days. The start-up costs associated with new service relationships are high, and would be an unreasonable burden on ILECs for such a short-lived contract. As the parties would simply have to go directly into renegotiations anyway, the better approach would simply be to negotiate a new, full-term agreement -- or to opt into an existing contract with more time left. This approach would be consistent with the language in Rule 51.908(c), which requires that interconnection agreements be made available only for a "reasonable period of time" after an agreement is approved and available for public inspection.[55]

Accordingly, the Commission should clarify that a CLEC may take service under an existing interconnection agreement only for the duration of the specified term, and may not choose to take the contract under a new, "refreshed" contract term. For example, an ILEC may agree to enter a three-year agreement beginning in 1997 to make existing services available until the year 2000. A third-party CLEC submitting a 252(i) request in 1999 should be permitted to adopt that same arrangement up until the year 2000 only. Unless such clarification is provided, this provision may be interpreted

[54] Interconnection agreements typically include renegotiation provisions which contemplate that the parties to the agreement will begin negotiating a replacement agreement within a specified period (*e.g.*, 90 days) prior to the agreed termination date.

[55] In no event should a carrier be permitted to opt into an *expired* contract, as the "reasonable" time for opting into that agreement surely would have passed. Moreover, ILECs are required, under Section 252(i), only those agreements "to which it *is* a party." 47 U.S.C. § 252(i); 47 C.F.R. § 51.809(a).

in a way that seriously and detrimentally impacts the ability of all LECs to negotiate binding interconnection agreements.

VI. CONCLUSION.

As set forth above, the Commission should squarely address the rampant market distortions and inequitable competitive results that have flowed from the imposition of "reciprocal" compensation obligations on ISP-bound calls that pass from ILECs to CLECs. The current approach has produced a lucrative arbitrage opportunity, which a growing number of CLECs have been able to exploit, and threatens to undermine key policy goals of the 1996 Act.

The Commission's tentative conclusion to allow the states to determine whether compensation should be paid for ISP-bound traffic would simply perpetuate these harms. Moreover, the Commission lacks the authority to delegate to the states its responsibility over interstate communications, including Internet access. Instead, GTE urges the Commission to take immediate action. While keeping the ESP exemption firmly in place, the Commission should declare an 18 month moratorium on payments between LECs relating to the delivery of ISP-bound traffic. During this period, the Commission should develop rules governing inter-carrier compensation for network access that: treat similar uses of ILECs' networks in a consistent manner; accurately reflect a carrier's actual costs; and allow for maximum flexibility in developing service and payment options for end users and ISPs.

As a final matter, GTE urges the Commission to clarify that a CLEC is not entitled to "opt into" an existing interconnection agreement for a full, "refreshed" contract term, under Section 252(i). Instead, the expiration date of such a new agreement would be the same as in the original agreement.

Respectfully submitted,

GTE Service Corporation and its affiliated companies

By: Gail Polivy

Thomas R. Parker
John F. Raposa
GTE SERVICE CORPORATION
600 Hidden Ridge
HQE03J27
Irving, Texas 75038
(972) 718-6969

Gail L. Polivy
GTE SERVICE CORPORATION
1850 M Street, N.W., Suite 1200
Washington, D.C. 20036
(202) 463-5214

THEIR ATTORNEYS

April 12, 1999